United States – Subsidies on Upland Cotton

(WT/DS267)

Executive Summary of the
Further Submission of the United States of America

October 14, 2003

1. **Brazil Has Failed to Demonstrate that Crop Insurance Payments Are "Specific."** The United States reiterates that the subsidy to any agricultural producer is the premium subsidy paid by the U.S. Government, which is common to all commodities at a chosen coverage level. Thus, Brazil's repetition that certain policies are not available to all commodities is in part true but wholly irrelevant: the particular *policies* offered to growers of different commodities are issued by private insurers but the *subsidy* by the U.S. Government on the premiums remains the same. Crop insurance subsidies are available to the U.S. agricultural sector as a whole. It is the position of the United States (reflected in domestic law) that such a widely available subsidy does not satisfy the specificity requirement of Article 2. Thus, pursuant to Article 1.2 of the Subsidies Agreement, U.S. crop insurance payments are not "subject to the provisions of . . . Part III" of the Subsidies Agreement, including Articles 5 and 6 on serious prejudice.

2. **Brazil Has Failed to Demonstrate that Challenged U.S. Measures Caused the Decline in World Upland Cotton Prices Because It Simply Ignores Key Factors Behind Those Price Movements**. Brazil has failed to make a *prima facie* case on its claims on the basis of the mere assertion that large U.S. outlays during marketing years with low prevailing upland cotton prices necessarily establishes causation. Brazil has failed to explain to the Panel key factors that affected world cotton markets during the marketing year 1999 - marketing year 2002 period. These factors and not U.S. subsidies were the causes of the dramatic plunge in cotton prices experienced in recent years.

3. **– Persistent weakness in world demand for cotton due to competing, low-priced synthetic fibers and weak world economic growth.** The production of competing, synthetic fibers exploded during the 1990's, putting downward pressure on world cotton prices. Asian countries added more polyester production capacity between 1991 and 2001 than existed in the entire world in 1990. Asian polyester prices remained below world cotton prices from 1990 to 2001. By 2002, cotton lost the position as the world's dominant fiber and slipped below polyester's market share. Consumer purchases outside the United States added over 40 million bales to textile fiber consumption since 1990 but virtually the entire amount was claimed by polyester. Consumers outside the United States buy no more cotton today than they did in 1990.

4. In addition to the price pressure from synthetic production, the world economy grew more slowly since 1997 than any time for many years. Clothing is a semi-durable good, and when income growth slows consumers cut back on current purchases, and postpone replacing clothing until incomes rise more rapidly. Cotton consumption can decline even while income growth remains positive. The 2001-2002 decline in world income occurred just as world cotton production was increasing because of good weather, severely pressuring world prices.

5. **– Burgeoning U.S. textile imports, reflecting the strong U.S. dollar and declining U.S. competitiveness in textile and apparel production, have fundamentally shifted the disposition of U.S. cotton production from domestic mills to export markets.** The United States has supported world cotton prices through its huge demand for cotton textiles and apparel. Imported textile and apparel products continue to displace U.S. mill use of cotton fiber. From 1997 to 2002, U.S. mill use of cotton dropped 32 percent. For 2002, U.S. cotton textile and apparel imports rose for the 14th consecutive year, while exports remained essentially unchanged

for the fifth straight year. This huge trade deficit in textiles and clothing has fundamentally changed the pattern of how U.S.-grown cotton is used. As domestic mill use has fallen drastically, more U.S. cotton has been available for use by foreign mills, which then comes back to the U.S. in the form of cotton products.

6. **– China, the world's largest cotton producer and consumer, released 14 million bales of government stocks between 1999 and 2002, equaling as much as 7 percent of world consumption in crop year 2000/01.** China's policies were strongly correlated to world cotton price movements through the late 1990's and early 2000's. Through the mid-1990's the Chinese Government was concerned with maintaining farmers' income and directed the state marketing organization to maintain cotton procurement prices at high levels, causing stocks to grow rapidly. At the beginning of the 1999/2000 marketing year, China announced a policy of auctioning cotton from these stockpiles, with the central government accepting the financial loss. China auctioned 11.6 million bales over August 1999 to July 2002 (3 million bales in 1999/2000, 6.5 million in 2000/01, and 2.1 million in 2001/02). Over the entire marketing year in 2000/01, China's auctions equaled 7 percent of world consumption that year.

7. **– Factors Affecting U.S. Cotton Production**. Cotton planting decisions are driven by numerous factors, including the expected price of cotton, prices of competing crops, farm program benefits, technological factors and input costs. Contrary to Brazil's claims, U.S. cotton producers have been responsive to world price movements and are not insulated from the world market. Changes in production technology can affect both the risk and the expected returns from cotton production. In recent years, the boll weevil eradication programs and the introduction and adoption of genetically modified varieties of cotton have lowered production costs, increased yields, and increased net returns for U.S. cotton production.[1]

8. Since 1994 there have only been 2 years when U.S. harvested acres changed from one year to the next in a different fashion than growers in the rest of the world. Those 2 years, 1998 and 1999, are specific to severe drought in the United States. In 1998, U.S. harvested area fell, largely due to disastrous conditions across much of Texas; in 1999, weather was more normal and U.S. harvested acres increased by almost exactly the acres lost in the previous year.

9. In early calendar year 2000, the futures price for cotton had fallen from the previous year's level while corn and soybean prices had risen on the year. U.S. and world cotton growers reduced harvested acreage from the level in 1999 by virtually identical proportions. While cotton harvest futures prices again declined on the year from 2000 to 2001, soybean and corn harvest futures prices fell by a greater percent. As a result, U.S. and world cotton growers saw an increase in cotton harvested acres in 2001. In considering planting in 2002, growers saw soybean

[1] Studies indicate that the boll weevil eradication program has lowered the costs of producing cotton and has made cotton a more attractive cropping alternative. U.S. producers have also rapidly expanded plantings of biotech cotton, rising from 25 percent of plantings during the 1997 crop year, to an estimated 73 percent of plantings in 2003. Studies suggest that biotech cotton has increased yields and net returns while decreasing pesticide use.

and corn harvest futures prices showing greater percentage increases than cotton. Thus, both U.S. growers and growers in the rest of the world saw harvested acres of cotton decline from the previous year's level.

10. **Brazil Has Not Established a *Prima Facie* Case With Respect to U.S. Decoupled Income Support Measures Because These Measures Have No More than Minimal Effects**. With respect to U.S. green box measures, namely direct payments under the 2002 Act and expired production flexibility contract payments under the 1996 Act, Annex 2 of the Agriculture Agreement makes clear that these payments have no, or at most minimal, trade-distorting effects or effects on production. Under Article 21.1 of the Agriculture Agreement, the Subsidies Agreement applies "subject to" the Agriculture Agreement. Accordingly, Annex 2 makes it clear that U.S. green box measures do not cause serious prejudice. Income payments that vary in amount with market prices, such as counter-cyclical payments under the 2002 Act and expired market loss assistance payments, are also decoupled in the sense of not being linked to current production. Because (according to the economic literature on decoupled payments) the effect on production is negligible, these payments can have no "effect" for purposes of Subsidies Agreement Article 6.3 nor operate to increase exports under GATT 1994 Article XVI:3.

11. Finally, because no production of upland cotton (or any other crop) is necessary to receive these payments, it would be erroneous to attribute to "upland cotton" or "upland cotton producers" all decoupled payments made with respect to upland cotton base acreage. Those acres may be planted to alternative crops or may be growing no crops at all. Accordingly, there is no basis to include those payments in an analysis of whether "subsidies provided to US producers, users and/or exporters of upland cotton" have caused serious prejudice.

12. **Brazil Has Failed to Demonstrate that Challenged U.S. Measures Have Caused Serious Prejudice to Brazil's Interests Within the Meaning of Article 5(c) and 6.3(c)**. – **"Serious Prejudice . . . May Arise":** The introductory sentence of Article 6.3 establishes that serious prejudice "may arise" if "one or more" of four specific circumstances is found, indicating that serious prejudice need not arise even if they are found. As serious prejudice "may" arise if one or more of the four conditions under Article 6.3 are satisfied, Brazil must first show that *at least one* of those conditions is met. Second, if Brazil demonstrates one or more of the criteria in Article 6.3 is met, Brazil must then demonstrate "serious prejudice." In this dispute, Brazil has not established that any prong of Article 6.3 is met.

13. **– The "Effect of the Subsidy":** Brazil has not made a *prima facie* case that "the effect of the subsidy" was significant price suppression or depression. Brazil's argument on causation fails because Brazil has simply not demonstrated the causal connection between the U.S. measures and the price effects. Brazil has not even shown there is a necessary correlation between the measures and the effects it claims, let alone that there is a genuine and substantial link between the U.S. measures and the effects claimed. Brazil has failed to separate and distinguish all the different effects from the various factors at play during the marketing year

1999 - marketing year 2002 period and has erroneously attributed to the U.S. measures the effects of these other causes.

14. **– "Significant Price Suppression"**: Article 6.3(c) requires that "the effect of the subsidy" is "significant price suppression." The Agreement does not define "significant." The ordinary meaning of significant is "important, notable; consequential," which suggests that the price suppression must reach a level at which it is important, notable, and consequential in order to be inconsistent with Article 6.3(c). The United States further notes that the term "significant" modifies "price suppression or depression"; therefore, it is the effect on *prices* that must be "significant" and not the direct effect on *producers*, as Brazil argues.

15. Under Brazil's interpretation price suppression would be significant at a level of even 1 cent per pound because this could still "meaningfully affect" producers. Brazil's interpretation, however, collapses the concept of "significant price suppression or depression" with the concept of "serious prejudice." It would also greatly expand the effect of Article 6.3(c), which falls under Part III of the Subsidies Agreement on "Actionable Subsidies" rather than Part II on "Prohibited Subsidies," to encompass *any* subsidy with any production and therefore price effect. Members agreed, however, that any theoretical price effect would not suffice to satisfy Article 6.3(c); they accomplished this by stating that the price suppression or depression had to be "significant" in order to create a situation in which serious prejudice may arise.

16. Brazil's theory would also create two sets of subsidy rules: one for widely traded products, such as most agricultural products, and another for more differentiated products. The more widely traded a product is, the more *any* price effect could be deemed to "meaningfully affect" producers. There is no basis in the text of the Agreement for creating such a distinction. Where Members intended a particular rule to apply to a particular type of product – such as a "subsidized primary product or commodity" (Article 6.3(d)) – they said so explicitly.

17. **– "In the Same Market":** Article 6.3(c) requires that the "significant price suppression [or] depression" that is the "effect of the subsidy" occur "in the same market." The use of the same "in the same market" phrase as in the price undercutting portion of this Article suggests that the significant price suppression or depression must occur when "the subsidized product" is found "in the same market" as "a like product of another Member." That is, "in the same market" is meant to require identification of a particular market in which price effects are alleged to have occurred so as to allow a comparison in that market. If a complaining party could merely assert price suppression or depression in the world market, the word "same" in the phrase "the same market" would be rendered inutile because the subsidized and non-subsidized products could always be deemed to be in the same "world market."

18. **– Time Period for Demonstrating Causal Effects**: The "appropriate representative period" for demonstrating present serious prejudice will depend on the nature of the challenged subsidies. Normally, the most recent period for which data are available will be the appropriate period. In the case of recurring subsidies such as those under the 1996 Act and the 2002 Act,

moreover, a past subsidy no longer exists as of the time a new subsidy payment in respect of current production is made and can have no "effect" within the meaning of Article 6.3. As a result, the period for which Brazil must demonstrate present serious prejudice is marketing year 2002. None of the provisions cited by Brazil, moreover, say that the effect of a subsidy 1, 2, or 3 years ago is presently being felt. Thus, at a minimum, the effect of the subsidy must be demonstrated in each year and for each year in which Brazil has alleged effects.

19. **Brazil Has Failed to Demonstrate that Challenged U.S. Measures Have Caused Serious Prejudice to Brazil's Interests Within the Meaning of Article 5(c) and 6.3(d) – "World Market Share"**: Contrary to Brazil's interpretation, Article 6.3(d) does not use the phrase "world market for exports"; it uses the phrase "world market share . . . in a particular subsidized primary product or commodity." This broad term would appear to encompass all consumption of upland cotton, including consumption by a country of its own cotton production. Context supports reading "world market share" as distinct from "world export share." In fact, GATT 1994 Article XVI:3 uses the phrase "world export trade," and Brazil interprets Article 6.3(d) and GATT 1994 Article XVI:3 both as applying to "world export trade." Had Members intended that "world export trade" be the relevant concept to apply in Article 6.3(d), one would have expected use of that phrase. Because Brazil has misinterpreted "world market share," and all of Brazil's evidence goes to a comparison of the "world export share" of the United States, Brazil has failed to make a *prima facie* case.

20. **– Appropriate Time Period for Showing Present Serious Prejudice:** Brazil has limited its claim under Article 6.3(d) to "the increased U.S. world market share for MY 2001." Thus, there can be no finding that subsidies under the 2002 Act or marketing year 2002 subsidies presently cause serious prejudice. As the United States has previously noted, to demonstrate the "effect of the subsidy" it would normally be appropriate to look to the subsidy provided in the most recent year. Brazil has not explained why it challenges marketing year 2002 subsidies (in addition to 1999-2001) under Article 6.3(c) but only marketing year 2001 under Article 6.3(d). Brazil has stated that the 1996 Act introduced a new subsidy scheme; at a minimum, Brazil should demonstrate that in fact there is a "consistent trend" over a period when subsidies have been granted (1996-2001).

21. **– Causation: "The Effect of the Subsidy"**: Brazil has simply not demonstrated the causal connection between the U.S. measures and the effects on world market share. As explained above, Brazil has failed to separate and distinguish other factors that drove prevailing upland cotton prices to historically low levels.

22. **Brazil Has Failed to Demonstrate any Inconsistency with GATT 1994 Article XVI:3 – "More Than Equitable Share"**: Brazil argues that in determining what is an "equitable" share, the Panel must look at what the U.S. share of world export trade would have been in the absence of subsidies. Brazil cites to no textual basis for its approach, nor could it since the text does not contain one. There is nothing in Article XVI:3 that says that a Member is banned from using any subsidies, let alone that a Member is denied the ability to have any share in world

markets if the Member employs subsidies. Any consideration of what is an "equitable" share needs to take into account the fact that Members are generally permitted to provide subsidies. However, any subsidy that has a production effect may increase exports; if so, according to Brazil, the resulting export share would be "inequitable." This interpretation would turn Article XVI:3 into a prohibition on subsidies that potentially could increase exports. Rather than imposing a prohibition, Article XVI:3 states only that Members "should seek to avoid" export subsidies on primary products, with additional conditions if inequitable shares result.

23. In considering the difficulties inherent in applying the "more than equitable world market share" language, the United States recalls the discussion of the Tokyo Round Subsidies Code panel on *Wheat Flour* on the "more than equitable world market share" language. The panel's enumeration of difficulties associated with this concept are the types of considerations that led to the negotiation of the Subsidies Agreement. Brazil now would have the Panel believe that these negotiations were unnecessary, that the disciplines it seeks were all in the language of Article XVI:3 all along. Brazil's approach is in error and should be rejected.

24. – **"Any Special Factors"**: Brazil considers that one "special factor[]" that may be affecting trade or that may have affected trade is the low level or even absence of domestic support in other supplying countries. Again, Brazil's proposed rule would suggest that where no other Member were subsidizing (each because of its own sovereign choice not to use resources in that way), a Member would be prevented from subsidizing in any amount that results in increased exports. However, Article XVI does not contemplate a prohibition on agricultural subsidies, even on export subsidies: under Article XVI:3, Members "should seek to avoid" use of export subsidies on primary products. Therefore, "any special factors" should not be interpreted in a way that introduces a meaning that the provision itself avoids.

25. **Brazil Has Failed to Demonstrate a Threat of Serious Prejudice**: Brazil argues that there is no explicit standard for threat of serious prejudice in the Subsidies Agreement nor guidance in WTO reports. The United States considers that the first standard articulated by Brazil is incorrect. Brazil's proposed rule would seemingly transform Articles 5(c) and 6 from actionable subsidy provisions into prohibited subsidy provisions. That is, Brazil's approach would produce a threat determination wherever "subsidies by a large exporter have no effective production or export limitations." There is no such *per se* threat rule in the Subsidies Agreement, however; a finding of serious prejudice requires a fact-intensive demonstration.[2]

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[2] The United States also considers that this proposed standard has not been met by Brazil. First, as explained above, Brazil has not established a *prima facie* case of present serious prejudice, and therefore one cannot presume that there is a threat such prejudice will continue. Second, the Appellate Body report in *United States – FSC* cited by Brazil involved export subsidies under the Agriculture Agreement and a completely separate standard. Under the serious prejudice provision of the Subsidies Agreement, the question is the much more complicated issue of what is the clearly foreseen and imminent effect of measures on a Member's interests, which may depend on future market conditions, world prices, and other factors. Third, Brazil has not demonstrated that the challenged measures are mandatory in the sense that they must be given if an application is made. Even though the Department

26. The United States believes the second standard proposed by Brazil is correct. To demonstrate a threat of serious prejudice a complaining party must show a clearly foreseen and imminent likelihood of future serious prejudice. The use of the elements of serious prejudice set out in Article 6.3 ensures that a complaining party come forward with sufficient credible evidence.[3]

27. – **Threat of Serious Prejudice Via Price Suppression**: In addition to the reasons just given, the United States notes that price developments over the past several months and expected price movements do not support a conclusion of a clearly foreseen and imminent likelihood of future serious prejudice. Brazil claims that "[b]ase[d] on MY 2002 prices, current prices in August 2003 and price levels projected by FAPRI's baseline, it is likely that marketing loan and CCP payments will be made during MY2003-2007." However, current market and futures prices (not reflected in Brazil's submission) already indicate that the baseline projection of low prices is wrong.[4] Thus, current prices and futures prices do not suggest any clearly foreseen and imminent likelihood of future serious prejudice.

28. – **Threat of Serious Prejudice Via World Market Share**: Brazil again reads "world market share" in Article 6.3(d) as the equivalent of "world export share." Thus, Brazil's threat analysis is wrong for the same reason as its serious prejudice analysis, and Brazil has not established a *prima facie* case of threat of serious prejudice under Article 6.3(d).

29. **GATT 1994 Articles XVI:1 and XVI:3**. Brazil asserts that the 2002 Act and 2000 Agricultural Risk Protection Act threaten a high and inequitable share of world exports between MY2003-07. Brazil nowhere cites the text of GATT 1994 Article XVI:3 (or of the Subsidies Agreement) that would support the notion that there is a valid cause of action for "threat" of a "more than equitable share of world export trade." In the absence of any text relating to Article XVI:3, Brazil's claim of a "threat" of a "more than equitable share" must be rejected.

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of Agriculture has the obligation to make such payments available, the obligation only attaches when certain market conditions prevail. Thus, to show that the threat of serious prejudice is (in Brazil's words) "real, clear, and imminent," Brazil would have to show predicted prices over the future period complained of (marketing years 2003-07) and the likelihood of that occurring.

[3] A similar concern is addressed for purposes of threat of material injury in countervailing duty investigations by Subsidies Agreement Article 15.7; under this article, "[t]he change in circumstances which would create a situation in which the subsidy would cause injury must be clearly foreseen and imminent." We note the relationship between threat of serious prejudice and threat of material injury, both of which make up part of adverse effects under Article 5.

[4] Instead of continued low prices, the A-Index *average* for September 2003 has risen to 64.06 cents per pound. New York Cotton Exchange futures prices demonstrate that market participants expect cotton prices to climb even further through the 2003 marketing year, strengthening beyond their 20-year average of 67.86 cents per pound (1983-2002) within the current 2003 marketing year. In fact, if cotton prices reach the levels (over 70 cents per pound) indicated by the futures market, prices would be very close to what Brazil calculates as the A-index average (74 cents per pound) for the period *before* Brazil alleges serious prejudice.

30. **Brazil Has Failed to Demonstrate that Challenged U.S. Measures Are *Per Se* Inconsistent with U.S. WTO Obligations**. Brazil argues that the marketing loan, counter-cyclical, direct, and step 2 payments as well as the crop insurance subsidies are *per se* inconsistent with U.S. WTO obligations because they threaten to cause serious prejudice at price levels that require the payment of marketing loan and CCP payments (that is, below 52 cents per pound). For all the reasons set out with respect to Brazil's present serious prejudice claims and its threat of serious prejudice claims, Brazil's argument is in error.

31. Brazil also argues that even at high price levels where only direct payments and crop insurance payments would be made, there is necessarily a threat of serious prejudice because these payments necessarily will keep marginal land in production because producers face no down-side revenue risk. Brazil has presented no evidence on the extent of any alleged effect of these two subsidies in keeping marginal production on-line at a time of high prices (as the market currently expects). Second, that some marginal lands may be kept in production cannot alone suffice to demonstrate a *per se* threat of serious prejudice. Otherwise, any subsidy with any production effect would be found to pose a threat, transforming actionable subsidies into prohibited subsidies. Thus, Brazil has not demonstrated that these subsidies *per se* present a real, clear, and imminent threat of serious prejudice.

32. **Export Credit Guarantees – The Negotiating History of Article 10.2 Reveals that the Negotiators Explicitly Deferred the Application of All Export Subsidy Disciplines on Export Credit Guarantees:** The negotiating history of Article 10.2 of the Agreement on Agriculture reveals the explicit deferral by the drafters of the application of export subsidy disciplines on export credit guarantees. In particular, the plain difference between the language of the Draft Final Act and that of Article 10.2 shows that the negotiators specifically opted not to impose the disciplines that Brazil now seeks to impose through litigation. The earlier version was an unambiguous prohibition, unless permitted under internationally agreed disciplines. The latter – and current – version imposes no such prohibition. It only requires Members to work toward the development of yet-to-be-agreed disciplines, and only upon agreement on such disciplines are export credit guarantee programs required to adhere to them.

33. Brazil's interpretation of Article 10.2 would require export credit guarantees in agriculture to be subject to more disciplines than any other practice addressed in the Agreement on Agriculture. Under Brazil's view, not only would export credit guarantees constitute export subsidies and be subject to all of the export subsidy disciplines, but Members would *also* be specifically obligated to work toward and then apply additional disciplines. Brazil's argument would require an interpretation that the negotiators viewed export credits, credit guarantees, and insurance programs as more malign than the recognized export subsidies themselves. This implausible conclusion is nowhere manifest in the text of the negotiating history.

34. To the contrary, the text indicates that export credits, credit guarantees, and insurance programs were not considered export subsidies, because they were explicitly excluded from

Article 9.1 of the Agreement on Agriculture, despite their inclusion in negotiating documents culminating in the current text. Brazil argues that the same is true of "[e]xport performance-related taxation concessions or incentives other than the remission of indirect taxes," and yet the Appellate Body has ruled the FSC and ETI measures are subject to the export subsidy disciplines of the Agreement on Agriculture. With respect to those measures, however, no provision like Article 10.2 exists. Export credits, credit guarantees, and insurance programs were not only removed from the illustrative list evident in Article 9.1 but received the explicit commitment to negotiate disciplines set forth in Article 10.2.

35. – **The Application of Government-Wide Accounting Rules under the Federal Credit Reform Act Indicates that the Export Credit Guarantee Programs are Covering Long-Term Operating Costs and Losses**: The United States has demonstrated that over time, as indicated by the government-wide accounting rules mandated under the Credit Reform Act, with respect to those years for which nearly complete experiential data is available, program revenues exceed operating costs and losses. In those years for which the accounting books are nearest to closing (1994 and 1995), the operation of the program shows a profit. Similarly, current data for 1992, 1993, 1996, and 1999 also indicate a profit. All of this data is on a cohort-specific basis, a methodology with which Brazil agrees.[5]

36. The United States has repeatedly noted that CCC has complete discretion at any time not to issue guarantees with respect to any individual application for an export credit guarantee or to suspend the issuance of export credit guarantees under any particular allocation. In addition, the authorizing statute prohibits CCC from making credit guarantees available in connection with sales of agricultural commodities to any country that the Secretary of Agriculture determines cannot adequately service the debt associated with such sale. Third, availability of export credit guarantees is governed by allocations in effect at any one time for specific commodities and specific destinations. Fourth, the ability of CCC to issue guarantees is constrained by the apportionment process of the President's Office of Management and Budget.

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[5] Brazil misapplies the cohort-specific accounting methodology, however, to erroneously argue that "when [the] total lifetime reestimates for all cohorts of guarantees disbursed since 1992 are netted against the total *original* subsidy estimates adopted each budget year during the period 1992-2002, *the resulting loss is nearly $1.75 billion*." To arrive at this fanciful figure Brazil begins not with the estimates based on the "actual" level of guarantees issued, but rather with the original subsidy estimate in the budget year, well before virtually any activity in the programs has occurred in that fiscal year. The "actual" figure is simply a reflection of the actual level of guarantees issued in the particular fiscal year. The original subsidy estimate, in contrast, begins with what is an historically overly optimistic projection of actual use of the program and then is required to use the government-wide estimation rules without regard to the actual experience specific to the CCC export credit guarantee programs.

Actual guarantee issuance can first be reflected only in the budget two fiscal years after the original subsidy estimate. Once the actual use of the program is determined all subsequent reestimates are based on that figure, not on the original subsidy estimate. Other than with respect to interest (because of independent market forces), a downward reestimate never occurs based on the original subsidy estimate. It only occurs subsequent to establishment of the actual program use. Consequently, it is wholly inappropriate to calculate net reestimates based on the original subsidy estimate for a particular cohort, as Brazil has done. For these reasons, the United States' calculation indicating increasing profitability within the program is accurate, and the Brazilian calculation is not.

37. – **Forfaiting is Analogous to the CCC Export Credit Guarantee Programs**: Brazil's argument that forfaiting transactions and CCC export credit guarantee transactions are dissimilar illustrates the comparability of the financing available in these transactions. As Brazil points out, in both cases "the exporter wants to get paid immediately on a cash basis, and the importer wants credit that it can repay on a deferred basis." From the importer's perspective, the export credit guarantee transactions are *less* favorable than forfaiting, because although the importer's bank can repay its obligation over time, the CCC has no control over the terms of the arrangement between the importer and its bank, which may not extend the deferred payment terms to the importer. In forfaiting, the importer "can repay on a deferred basis." In both cases, the transaction (in Brazil's words) "enables the exporter to convert a credit sale into a cash sale." Brazil recognizes that as the complaining party it carries the burden of demonstrating that a "benefit" is conferred with respect to the GSM-102 program. Brazil has failed to carry this burden.

38. **The Step 2 Program Does Not Violate Article 3.1(b) of the Subsidies Agreement or Article III:4 of GATT 1994**: Brazil has rotundly stated: "There are no circumstances in which a 'local content subsidy' would comply with Article 3.1(b)." In effect, Brazil's argument would delete the application of the introductory clause of Article 3 to Article 3.1(b) entirely. But the phrase "except as provided in the Agreement on Agriculture" by its terms applies to both export subsidies under Article 3.1(a) and local content subsidies under Article 3.1(b).

39. Brazil would require the Step 2 program to permit payments for the use of all cotton, whether domestic or imported, but only payments for domestic cotton would be included in the AMS. Such a program would no longer be in favor of domestic producers. The Step 2 program provides a benefit to producers because it serves to maintain the price competitiveness of U.S. cotton vis-a-vis foreign cotton through a payment to capture some differential between prevailing foreign and domestic cotton prices. Brazil's hypothetical program would cause the benefit to U.S. producers to evaporate. Rather than a subsidy "in favor of agricultural producers," the program would become a simple input subsidy in favor of textile manufacturers outside the coverage of the Agreement on Agriculture altogether. Brazil's interpretation would render Paragraph 3 of Annex 7 of the Agreement on Agriculture inutile.

40. Brazil argues that since the Peace Clause provisions for domestic subsidies do not reference Article 3, the Agreement on Agriculture envisioned that local content subsidies would be prohibited. Brazil's conclusion does not necessarily follow from the structure of the text. Indeed, a contrary conclusion is more appropriate. Article 13(b) does not refer to Subsidies Agreement Article 3 because the substantive obligation of Article 3.1(b) does not apply in the case of domestic content subsidies in favor of agricultural producers. Article 13(b) applies to "domestic support measures that conform fully to the provisions of Article 6 of this Agreement." The character of the domestic subsidy is not relevant to the disciplines. The Agriculture Agreement never defines "domestic support," which is permitted in any form so long as the Member adheres to its reduction commitments.